THE NATIONAL CITY BANK OF NEW YORK

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Economic Conditions
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United States Securities

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General Business Conditions

THE course of business has been upward since the middle of March, and considering the severity of the disturbance in the economic system caused by the banking panic the recuperative power displayed has been decidedly encouraging. It had been feared that the tying up of deposits in closed banks would depress business indefinitely, and apprehensions had been expressed that the situation would lead to increased commercial difficulties and distressed selling. But these fears proved unfounded. The financial situation has improved, as described later in this Letter, and the rapid drop in the volume of trade and industrial production that occurred early in March has been followed by a rise of equivalent proportions, quickly regaining the lost ground. Moreover, commercial failures instead of increasing have decreased remarkably; the total in March was the smallest for the month in eight years, according to Dun & Bradstreet, and this good showing has continued during April.

Steel mill operations have had a pronounced revival, rising from 14 per cent of capacity in the third week of March to 25 per cent in the last week of April, according to the Iron Age estimates. This is five consecutive weeks of gain, and brings operations to the highest point since March, 1932; and this is the first time in four years that steel operations have been higher than one year previous. While orders for automobile materials have been the chief gain, a satisfying improvement in miscellaneous demands is reported. At 25 per cent the steel industry is not as far away from profitable operations as may generally be believed. The Chairman of the Republic Steel Company, Mr. T. N. Girdler, stated at the annual meeting that by reason of drastic economies the company could now make money on 35 per cent operations, and maintain its cash position at a rate of 25 per cent or slightly less. There is reason to think that this showing is typical of the industry, illustrating the influence of the depression in reducing costs.

Automobile sales snapped back smartly after the bank holiday, and General Motors' sales to consumers for the whole month of March were only 2.6 per cent below the same month of 1932. April sales have made a good gain for most companies, and production has been sharply increased. To be sure these gains, and the steel improvement also, are mainly seasonal in character, but there was no lack of prophecy during March that not even the seasonal gains would be realized.

Building continues to be the chief laggard among the industries. Contracts awarded during March, on a daily average basis, declined below February instead of making the usual rise, and during the forepart of April the figures showed no improvement. The level of building activity is but half that of last year. Despite this poor showing lumber orders have picked up, and in the week ended March 25 were greater than in any previous week of 1933 or 1932, except for two weeks last September. Orders from the brewing industry are mentioned as a factor in the lumber demand, and also in other markets.

Merchandise car loadings, like steel production, have increased for five consecutive weeks, and this seasonal gain is encouraging inasmuch as it did not appear last year. The figures are making a better comparison with 1932 than heretofore, which is likewise true of electric power production, another good index of general business.

Mercantile trade picked up after the middle of March under the joint influence of the approach of Easter and the reopening of the banks, and the improvement has continued. The Easter retail trade was better than had been expected, in view of all the circumstances. In wholesale markets the advance in commodity prices has stimulated demand. The volume in all the textiles has been large, and the movement of spot merchandise brisk. However, there is no evidence that the inflationary developments have led to heavy speculative buying by retailers. Their attitude is generally described in the market reports as one of watchful waiting. Textile mills in many cases have been unwilling to accept orders for late delivery, in view of uncertainty as to prices.

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Amid all the inflation talk, this genuine improvement of business should be recognized. It is evidence of a power of recuperation which the pessimists, and those who have held that inflation is the only way out of the depression, have been too ready to deny. Business is nothing more than the satisfaction of the wants of the people by the production and exchange of goods and services, and as long as wants are unsatisfied the recuperative power is always latent. It is the natural instinct of business men to do business. Everybody wants to do business and this is a powerful force for enlarging trade. The problem of getting out of the depression has never been a problem of applying a stimulus to business, but of removing the obstacles which have held it back, interfered with the exchange of goods and services, and curbed the natural enterprise of the people.

Foreign Exchanges and the Markets

The rise in the markets and the fluctuations in the foreign exchanges during the month have been spectacular, and since they have occupied the front pages of the newspapers, require but brief description. The dollar dropped more than 10 per cent in the exchanges, with French francs rising as high as 4.48 cents compared with their par of 3.92 and the pound sterling advancing to $3.93 compared with about $3.40 in the forepart of April. With this moderate depreciation the decline of the dollar was checked, and the strengthening effect of the normally favorable balance of payments came into play.

Before this depreciation occurred the prices of stocks and commodities had begun an orderly upward movement; and upon these developments they rose sensationally. Naturally prices of products entering the world markets advanced to offset the decline in the dollar, and there was a general rise in other staple commodities and in equities, discounting the steps taken in the direction of inflation. The advance paused as the dollar ceased to decline, but the gains have been substantially held. The extent of the price movements during the month is shown in the following table giving various price indexes:

	April 1	April 25	Percent Change
Commodities (Moody's daily index of 15 staples)	86.4	102.2	+18.3
Stocks (Dow-Jones averages)			
30 industrials	55.66	72.45	+30.2
20 public utilities	19.38	23.28	+20.1
20 rails	25.06	30.11	+20.2

Rise Not Wholly Inflationary

Looking back to the banking crisis in March, and to the fears that the resulting financial situation would exert a deflationary pressure upon prices, this is a dramatic change in the markets, and of course a very important one. The gains in commodity prices have been centered precisely where they will do the most good, i.e., in the farm products and industrial raw materials, which represent the income of millions of producers, and which have been so depressed that their purchasing power over manufactured goods has been almost destroyed.

Moreover, the advance has not been solely due to the inflationary developments, and to ascribe it entirely to them is to misjudge the situation. Both business improvement and changes in the market position of various commodities have been factors. The grains have led the rise, and no inflation explanation is necessary to account for higher grain prices in view of the short wheat crop. The advance in sugar has a strong statistical basis. The rise of wool, hides and silk has the support of an improved statistical position. The decision to shut down domestic mines is a factor in copper. Scrap steel has risen in Pittsburgh by $1.50 a ton, and pig iron in some markets by $1 to $2; and this signifies a short supply and a better demand from the steel makers, who are selling more steel to automobile manufacturers, who in turn are selling more cars; and these sales are accounted for not by expectation of inflation but by a desire and need for automobiles.

In short, in various commodities there has been given a demonstration that prices are responsive to supply and demand, and that the combination of decreasing stocks, low production and low prices eventually overcomes the causes of the price depression. In the confused economic situation, wherein the guideposts are difficult to follow, this demonstration is both heartening and instructive.

The Advance in Wheat

An encouraging aspect of the advance in commodities is that it has been led by wheat. Wheat is a very important commodity in this country, not only because it is one of the two chief cash crops but because its fluctuations affect the other grains, and greatly influence the sentiment of the farm communities and all who sell to them. The first estimate of this year's Winter wheat crop issued by the Crop Reporting Board on April 10 was a very bullish document, placing the yield at only 334,000,000 bushels, the lowest in twenty-nine years. The market was prepared for a low figure, and had already advanced substantially; but this estimate was 35,000,000 bushels below the private reports, and the rise was immediately resumed, carrying the price of May contracts in Chicago before the end of the month to nearly 70 cents. This is a rise of 51 per cent in eight weeks.

This is the most significant change in the wheat situation in this country in a good many

years. The period from 1927-28 to 1931-32 was one of constantly increasing wheat supplies, due to production in excess of domestic requirements and declining exports under the Farm Board regime; and the end-season carryover rose each year, from 133,000,000 bushels on July 31, 1928 to 370,000,000 on the same date last year, despite heavy feeding to livestock in the last two years of the period. During the present season, ending next July, this accumulation of supplies has been checked, due to last year's short crop, but the carryover will be only moderately reduced.

Next season, however, the statistics will show very differently. If the present estimate of Winter wheat holds and the Spring wheat yield is around the average, the total crop will scarcely exceed 600,000,000 bushels, which is below the domestic requirements in any year since 1922, and compares with an average domestic use of about 725,000,000 in the past three years. Allowing for small exports, there is a possibility that the surplus may be reduced 150,000,000 bushels by the end of next season, and brought below 200,000,000 for the first time in six years. Of course the speculators are looking forward to this decrease in the supply, and at the risk of their capital are making the higher price available to the farmer before the rise would otherwise occur.

The world statistical position is not improving during the current season, but the improvement in this country will help the world situation next season. The indications are that Russia will not be a factor in the markets. The European countries will harvest an acreage of Winter wheat approximately the same as last year, and crop prospects are favorable. The Canadian crop, and the Argentine and Australian plantings, of course remain factors of uncertainty.

Causes of the Rise in Sugar

Another commodity which has given leadership in the price advance is sugar, which has risen in two months from 0.65 cents per pound for Cuban raws, less duty, to a peak of 1.35 cents on April 25. Sugar has been of all commodities the worst buffeted by the post-war shifts of production, resulting from the endeavor of importing countries to grow their own supplies. Of course these efforts were at the expense of exporting countries, which had expanded their producing capacity to meet the wartime demands, and as a result the sugar industry was prostrated long before the general collapse occurred.

Under pressure of their necessities the exporting countries worked out the Chadbourne plan, calling for drastic reduction of their output and exports. To bring the plan into effect was naturally a slow process, since in countries like Cuba, practically dependent upon sugar, it compelled very severe readjustments in the national economy. However, the great distress of these countries was an incentive, and this year the output of the principal exporters has been sufficiently reduced to assure a substantial decrease in accumulated stocks. The following table gives the trend of sugar production in the exporting, importing and self-sustaining countries, and shows the drastic reduction in the exporting countries this year. A further sharp decline in the Java crop next season is expected.

SUGAR PRODUCTION

Thousands of Long Tons

	Average 1909-13	Average 1922-26	1930-31	1932-33
Exporting Countries	7,376	10,524	11,750	6,653
Cuba	1,903	4,422	3,122	2,000
Java	1,309	2,004	2,799	1,300
5 Countries of Europe	3,914	3,513	4,964	2,511
Importing Countries	4,417	6,534	8,875	10,914
U. S. & Possessions	1,793	2,458	3,617	4,188
British Empire	2,624	4,076	5,258	6,726
Self-sustaining Countries	2,533	3,968	5,920	5,399
Japan	192	506	929	940
TOTAL CROP	16,572	21,750	28,454	24,255

Stocks of sugar in the exporting countries, except Java, are now below last year's level, and it is estimated that world consumption this season will be around 26,750,000 tons, or above 2,000,000 in excess of the production. This substantial change in the situation gives ample reason for the price advance. The quotation for Cuban sugar at New York includes such charges as transportation, ocean freight, insurance, bagging, export tax and selling expense, and with these deducted the low price of 0.65 cents represented a net price at the Cuban mill which was less than the out-of-pocket cost of harvesting the cane and manufacturing it into sugar, disregarding the cost of growing the cane and all other cost factors. Of course this situation could not last.

The Gold Embargo

The order of President Roosevelt on April 20 prohibiting until further notice exports of gold from the United States, or earmarkings for foreign account, marks a momentous change of national policy, and signifies a turn to inflationary methods in the effort to find a way out of the depression. Coming at a time when the country's gold holdings are close to record figures, and when its receipts on international account exceed its payments except as flight of capital may temporarily reverse the balance, this action is in no way comparable to the unwilling abandonment of the gold standard by countries having a continuously unfavorable balance of payments. On the contrary, it is everywhere interpreted as a deliberate stroke of policy, and as but one part of a broad program to raise prices. The fall of

the dollar to a discount in terms of gold currencies is a consequence of this view.

A gold embargo had been declared during the financial crisis in March, as a measure to preserve the banking resources; but at that time the economy program and the vigorous handling of the crisis maintained confidence in the dollar, and except for an initial flurry its value in the exchanges was not affected. Thereafter, when the growing consideration given to inflationary proposals in this country again led to sales of dollars, driving the exchanges to the gold point, the Treasury issued licenses for a number of gold shipments, making the embargo seemingly a dead letter. However, the distrust grew and the weakness of the dollar persisted, culminating in a rise of the gold currencies substantially above the gold export point.

Obviously this situation demanded a decision by the Administration either to take a position that would allay the distrust, and continue gold payments, or to divorce the dollar from gold. Presumably upon the theory that with the currency divorced from gold the domestic price level could be advanced above the gold price level, this momentous decision was made, carrying the United States voluntarily off the gold standard to join the company of many other countries that have gone off involuntarily since the depression began.

Authority to Expand Credit or Currency

Complementing the gold embargo, the President at once asked from Congress authority to put into effect, in his discretion, a number of stated inflationary measures, beginning with an expansion of Federal Reserve credit by requiring the Reserve Banks to purchase up to $3,000,000,000 of Government securities in addition to those they already hold. The effect of these operations would be, first, to provide credit for Government expenditures to the amount of new securities purchased, and, second, to increase the reserves of the member banks, and consequently their ability to make loans and investments. It should be understood, however, that if banking reserves created in this way are to be put to use it is necessary that there shall be a demand for loans by business men of good credit standing, or that investments shall be available in which banks have confidence. The Reserve Banks engaged in such an operation last year, purchasing $1,085,000,000 of Government securities, with results giving little assurance that prices can be raised by this means.

The act recognizes the possible ineffectiveness of this effort, and provides that if it shall be considered unsuccessful an issue of Treasury currency for the purpose of paying Government obligations in the amount of $3,000,000,000 may be made, the currency to be redeemed in twenty-five years at the rate of 4 per cent of the total issue per annum. This is the fiat money route to inflation. The plan applies controls in the limitation of the currency issue and the provision for its redemption. However, if one Congress could pass this act another Congress could revise it; and if any such amount of currency should be issued it is extremely unlikely that it would ever be retired in the manner described, since to do so would impose a deflationary influence on the country over the entire period of the operation.

As a final recourse, and with the return to the gold standard in mind, the President is given power to reduce the gold content of the dollar by not more than 50 per cent. He is also authorized to provide for the free coinage of silver, in such ratio to gold as he may proclaim. Another provision of the act authorizes the acceptance of intergovernmental debt payments in silver at a price not over 50 cents per ounce, in an amount up to $100,000,000, and the issue of currency against this silver.

This sweeping act defines the policy of the Government in indisputable terms as an intention to raise prices, and confers powers upon the President designed to be sufficient for that purpose. Removing the currency and credit systems from the automatic discipline of gold, and substituting the management of the executive authority, it places upon the President the full responsibility for the execution of this program. Likewise it lodges with him the responsibility for the control of the inflationary forces, if once they are loosed.

The Conflicting Views on Inflation

The conflicting views upon the policy of inflation differ sharply over the part of money in the economic system. The inflation theory is based upon the idea that money is the motive power that makes business go, and that the depression is due to a lack of purchasing power circulating among the people.

The opposing view holds that money is not the chief motive power in the business world, but only a part of the mechanism of the exchanges. It emphasizes that the products and services moving in trade pay for each other, that the great body of trade settles itself, as seen in the immense volume of bank clearings, in comparison with which the amount of money in circulation is insignificant. Disorder in trade relations has blocked the flow of goods into consumption, caused the unemployment and brought on the fall of prices.

The currency supply is automatically provided by twelve Reserve banks, located in different parts of the country for that purpose. They supply the member banks and the latter supply their customers. The facilities of distri-

bution are ample, but at last the circulation of money among the people depends upon employment and trade. Money is the servant of trade, but trade is free and full or restricted and depressed according to the terms upon which exchanges can be made—in other words according to price relations, as, for example, between farm products and manufactures, transportation costs, etc.

If this is a correct explanation of the cause of the depression, the situation calls for readjustments where disorder exists rather than for an influence of general and incalculable effects, as is that of monetary inflation. There is need for the guidance of the law of supply and demand, which acts always to maintain or restore order in the economic system. An eminent Senator said in the recent debate that the law of supply and demand had failed to be effective in the case of wheat, but that commodity affords a conspicuous example of blind or misguided interference with the normal operations of supply and demand.

The influence of inflation would affect all prices and economic relationships, and although all would not be affected alike, because of different conditions, that of itself increases the uncertainty of results. The monetary system and banking reserves already have the capacity for handling as large a volume of business as in 1929, at as high a price level, and if a progressive program should be adopted for increasing this capacity until the desired price level was obtained, the ultimate results might be far beyond anything contemplated. It is unnecessary to cite the experience of Germany and other countries with inflation. The experience of the United States from 1914 to 1929 with inflation on a gold basis under so excellent a control system as that provided by the Reserve Act, teaches a lesson of profound import.

What would be the effect upon the creditor class? For after all the creditor class is not an enemy class. Credit is a necessity of modern economic life, and cannot be ruthlessly destroyed, without injury to all classes. The debtor should be protected, but the millions who by reason of their labor and savings have gained a creditor position are entitled to a like assurance of justice.

Inflation is unjust because its influence is sweeping, affecting all debtor-creditor relations without regard to varying conditions and real equities. Many billions of outstanding obligations originated back of the war period; in many instances the circumstances are such that neither hardship nor injustice to the debtor is threatened, and in vast numbers of cases both hardship and injustice would result to creditors from a uniform scaling down of obligations. The effect would be to make arbitrarily a vast transfer of property values on the strength of conditions that there is reason to believe are in large degree temporary.

What would be the effect upon the wage-working class, which holds a creditor position? The American Federation of Labor gives notice that it will demand wage-advances to correspond with any rise of the cost of living. The wage situation therefore would be in confusion. The wage-workers are as much interested as any class in the reestablishment of conditions which will restore employment for all, but they are wise to be on the alert when inflation is proposed. They can far better afford to make definite wage concessions which are covered by lower living costs than to be subject to the uncertain effects of inflation.

It is urged that inflation is necessary to overcome the effects of deflation, which is said to result from all downward readjustments. The answer to this is that orderly readjustments in the industries, which will restore the equilibrium, will not diminish the aggregate of purchasing power, but increase it; they will revive the flow of the exchanges, which means the reciprocal exercise of purchasing power. With the industries in balance, the millions of would-be workers who are idle would be creating and using purchasing power. And that is the sound way to raise prices.

Other Measures to Promote Recovery

Along with the price-raising program, the Government is undertaking measures for business recovery which may be described as a combination of adjustments to restore the balance in economic relationships, of relief for distress, and of activities to stimulate employment. The chief of the adjustments is the reduction in the cost of operating the Federal Government. Making use of the powers granted in the economy act, President Roosevelt has ordered decreases in pensions and other veterans' compensations and a cut of 15 per cent in Federal salaries, which he finds justified by the reduction of 23 per cent in the cost of living since 1928; and has also directed the consolidation or elimination of governmental activities in many quarters. In total these reductions are expected to save a billion dollars or more.

This is an achievement evoking unqualified approval and admiration, both for the nature of the program and the method of its execution. It disposes of the fiction that Federal expenditures could not be reduced, and strengthens the Government credit in a degree which is of incalculable value, considering that the Treasury will continue to borrow for relief and other purposes. Whatever the extraordinary expenditures that may be undertaken, it

can no longer be maintained that the fixed expenses are out of control.

The proposal for the refinancing of farm mortgages through the Federal Land Banks is another measure of readjustment. The essence of this proposal is that the Banks may issue up to $2,000,000,000 in bonds bearing not over a 4 per cent coupon, with interest guaranteed by the Government, for the purpose of acquiring farm mortgages by purchase or exchange. No mortgage is to exceed 50 per cent of the normal value of the land and 20 per cent of the value of the improvements. The rate of interest on the mortgages is reduced to 4½ per cent during the next five years, and principal payments are deferred for that period if the buyer is not otherwise in default. A bill of similar character with respect to small home mortgages is likewise on the Administration's program.

In effect these bills would require the holder of a mortgage, who wishes to exchange it for a bond with guaranteed interest, to accept a reduction in the interest rate on the obligation, and almost certainly in the face value also. This writing down of values is a realistic policy, fitting the situation, and the whole program should aid in relieving the disturbance and uncertainty resulting from this troublesome problem. There is no tax on the Treasury save for the contingent liability as to interest, and since the amount of Government credit put out will be less than the amount of private credit it replaces, this method of treatment cannot be described as inflationary. On the other hand, we see little merit in the argument that it is deflationary. It but recognizes a deflation which has already occurred, since the values marked down have already disappeared.

These refinancing plans may have great social value. A comment is made by Anderson, Clayton & Co., which should have general endorsement: "Farmers have suffered for years financially, but they need not be unemployed or hungry as long as they can stay on their farms. The only immediate farm emergency is to prevent the unsocial ejection of good farmers from their farms." The leading life insurance companies have suspended foreclosures on owner-occupied farms for an indefinite period. This is a departure from the established rights of private property, but considering the severity of the times the action is a wise and tolerant one. It is not in the general interest that there should be sweeping transfers of the ownership of property under these abnormal conditions.

It is the understanding that a bill is in preparation which will include provisions to facilitate the writing down of the railroads' indebtedness, as part of a program of railway rehabilitation, and will also provide for economies leading to a reduction in railway expenditures.

The Position of Creditors

All of these measures—and the policy of closing insolvent banks is another which may be included—have in common the fact that they face the realities of depreciated values and unbalanced relationships, recognize them frankly, and take the natural way out, which involves the acceptance of losses by creditors, and reduction of wage and interest rates and other items of cost. The effect is to remove barriers to recovery. But what is now to be said, in view of these measures, for the argument that nothing but inflation can remedy the injustice which the price decline is declared to have worked against debtors and in favor of creditors? Should the creditor who foregoes legal rights and assents to a plan for the relief of the debtor then be penalized additionally by an inflation which will reduce the value of the remaining return from his investment, by reducing its purchasing power? Should Federal employes and other workers, who have had their pay cut to accord with a lower cost of living, then be subjected to an inflationary increase of living costs, on the plea of relieving the debtor?

These are questions of economic as well as ethical significance, for all students of the question recognize that the essential quality of prosperity is in balanced relationships; and if relationships are brought into balance by one measure and thrown out by another, the restoration of prosperity has not been promoted. The fact that the program of the Government includes these readjustments is a very important consideration. It has served to maintain confidence that an Administration which has seen the situation in this light and carried through the policies described will exercise its inflationary powers with restraint and under careful control.

Relief and Government Works

The second group of measures in the Administration's program is for the relief of distress. Of these only the act establishing the Civilian Conservation Corps, a method of relief not before tried in this country, has been brought to passage. This calls for the organization of 200,000 to 300,000 unemployed virtually along military lines, whereby they will be housed and fed in camps, employed in reforestation, drainage and similar conservation work, and paid not to exceed $30 a month, part of which will be allotted for the assistance of their families at home. This plan is more expensive than direct relief, but if the work done is useful and productive it has a great deal to commend it, and is in every respect superior to the expenditure of large

sums by the Government on non-productive public works at normal wage rates. It is a sound principle that the relief wage should be lower than wages in private industry. It assures that the relief expenditures will not be continued longer than necessary, for the men will seek private employment as rapidly as opportunities offer. The government cannot long give employment to any considerable fraction of the unemployed, and it is well that the relief set-up should impose a natural check to such employment. Labor need not fear that normal wage scales or living standards will be imperilled by this measure, which applies only to relief work and not to private enterprise.

In addition to the provisions for relief, proposals are being urged upon the Administration to create work by Government expenditures, by the use of Government credit to promote private enterprise, or in other ways by the exercise of Government authority. Some of these proposals have been embodied in bills introduced into Congress.

The general theory of Government expenditures on public works or of subsidies to private enterprise is that they will give a start to business, or "prime the pump" as the expression is. Undoubtedly Government works will give employment and create trade as much as any other enterprise, but the Government cannot possibly carry on sufficient work of its own to make up for the decline in private employment and trade; and while its activities will aid private industry while they last the effects will not continue after the expenditures cease unless private industry meanwhile is reestablished on a self-supporting basis. The theory of priming the pump assumes that the pump is in order, but if that were so the pump would need no priming, and if it is not in order no amount of priming will make it produce water. Of course it is the theory behind the turn to inflation that a rise in the price level will put the pump in order, but the hazard is involved that more and more stimulus will be required to keep it working.

Another feature of the program that is being debated in the Congress is the thirty-hour work week bill, which is aimed to reduce unemployment, but would so raise production and distribution costs as to force further curtailment of industry and more unemployment. We refer readers to a discussion of this proposal in a subsequent article in this Letter.

Money and Banking

The banking system during the past month has made further rapid progress in overcoming the effects of the panic. Money "in circulation"—that is, outside of the Federal Reserve Banks and Treasury—declined sharply during the month and on April 19 was nearly $1,500,000,000 below the March peak.

From the movement of currency over the past month it is clear that the country is in need of no additional issues of currency. Trade is not using the money that is already at its disposal, as indicated by the return of money to the banks for deposit. Should further issues of currency be made it is evident that they would not stay in circulation, but would promptly pile up further excess funds in the banks, where the volume of funds already is far greater than the banks are able to lend upon proper security. With the facilities for expansion provided by the emergency banking act passed a month ago the banking system has almost unlimited capacity for issuing currency already. Very little, however, of this new currency has been issued, for the reason that there has been no demand for it. According to the Federal Reserve statement of April 19, the amount of the new Federal Reserve bank note currency outstanding on that date was only $25,000,000, and this, of course, has been far more than offset by the return of other forms of currency since the end of the bank holiday.

The Increase of Gold Stocks

Of the $1,500,000,000 or thereabouts of money returned to the banks since their reopening, over $600,000,000 was in the form of gold and gold certificates, and these deposits, together with some return of gold from foreign holders, have immensely strengthened the position of the Federal Reserve Banks. At $3,366,000,000 on April 19, gold reserves of the Reserve Banks were up $682,000,000 from the March low point, and at the highest level on record, excepting only a few months in 1931 just prior to the panic that followed Great Britain's departure from a gold basis. On April 19 the ratio of reserve to combined deposit and note liabilities of the Reserve Banks stood at 61.5 per cent, compared with 45.6 on March 8.

Figures on the total stock of gold money in the country show less of a recovery than the Federal Reserve figures alone, by reason of the fact that the return of gold shipped abroad or earmarked for foreign account was considerably less rapid than the recovery of gold from internal circulation. Nevertheless, because of the greater concentration of the gold supply in the Federal Reserve Banks, the effectiveness of these stocks as a basis for credit has been greatly increased. Including the stock of $1,657,000,000 gold belonging to the Treasury and the $2,255,000,000 held by the Reserve Banks, the volume of gold under direct control of the monetary authorities of this country continues larger than that of any other country, exceeding the French holdings

by $734,000,000, and comprising approximately 33 per cent of the total gold stocks of central banks and treasuries of the world.

Following is a table showing figures of gold and circulation by weeks:

(In Million Dollars)

Week Ending	Money in Circulation	Gold Reserves of F. R. Banks	Gold Stocks of F. R. Banks and Treasury	Total Monetary Gold Stocks*
Feb. 1	5,652	3,255	3,477	4,548
8	5,705	3,247	3,458	4,535
15	5,854	3,200	3,405	4,511
21	5,988	3,118	3,341	4,460
Mar. 1	6,720	2,892	3,102	4,344
8	7,538	2,684	2,894	4,243
15	7,269	3,011	3,236	4,251
22	6,608	3,192	3,435	4,264
29	6,353	3,237	3,505	4,272
Apr. 5	6,261	3,279	3,539	4,283
12	6,147	3,315	3,567	4,293
19	6,068	3,366	3,606	4,313

*Includes gold in circulation.

Money Again Easier

With currency and gold flowing back into the banks and augmenting basic reserves, the last vestiges of monetary strain have been disappearing from the financial centers. Member bank rediscounts with the Federal Reserve are down something like 70 per cent from the peak for the country at large, while holdings of bills purchased by the Federal Reserve are down about one-half. Both at New York and Chicago member banks are again completely out of the Reserve Banks. With indebtedness reduced, excess reserves are again accumulating, and on April 26 amounted to $192,000,000 for New York banks and $62,000,000 for Chicago banks.

Reflecting the foregoing developments, money rates have dropped down to levels approaching the low points of January, as indicated by the following table comparing the January lows with the March high points and the latest quotations.

	Per Cent Jan. Low	Mar. High	Latest (Apr. 25)
Call Money	1	5	1
Time Money	1½-¾	4	1-1½
Commercial Paper	1¼-1½	4½-4¾	2½-3
Bankers' Acceptances*	¼	3⅝	½

*90 days—asked.

The Trend of Bank Credit

Bank deposits have gained steadily since the bank holiday, and on April 26 the figures for New York banks were nearly $800,000,000 above the low levels reached during the panic. While figures for interior banks are not available owing to the fact that the condition reports of all weekly reporting banks have not been published since the holiday, a steady rise in the volume of bankers' balances at New York to a point about $450,000,000 above the March low is indicative of a general improvement of banking conditions in the interior as well. The chief difficulty continues to be to find secure employment for the large amount of funds available. Loans and investments of the New York banks have increased only $100,000,000 since March 15, and all of this occurred during the single week of April 26.

Should the Federal Reserve Banks embark upon an extensive campaign of further Government security buying, as contemplated in the new banking bill before Congress, it is clear that the volume of excess bank reserves will be still further enormously increased. And if the Government goes further and issues large amounts of currency, the effect will be the same, for the currency, being unwanted by trade, is bound to find lodgment in the banks which in turn will deposit it in the Reserve Banks for credit to their reserve accounts. Whether such increase in the volume of reserves will actually be translated into a larger volume of bank credit in use, and so become an influence in raising prices, is a debatable question. As we have already indicated in a preceding article, the existence of a large excess of bank reserves in 1932 did not have that effect. While it is probably true that if the determination to inflate credit is pushed far enough it may eventually be successful, there are reasons for fearing that not all the consequences of such a policy would be desirable.

Exchange Stabilization

Accounts more or less sensational have appeared regarding the operations of the British "Exchange Equalization Fund," and the resulting increase of approximately $300,000,000 in the gold holdings of the Bank of England since January 1st last. Some of them have described an imagined conspiracy against the trade of the United States, which has no other foundation than that numerous countries are off the gold basis and that depreciating currencies exert a demoralizing influence in world trade.

The conditions under which Great Britain suspended gold payments in September, 1931, were well known at the time, and it was recognized to have been an unwilling and unavoidable act. In the absence of the gold basis for exchange relations the foreign exchanges of Great Britain naturally became unstable, first declining from the par, $4.8665, to about $3.25 in less than three months and then rising to about $3.83 in about the same length of time.

In his budget speech in Parliament on April 19th, 1932, the Chancellor of the Exchequer asked for authority to borrow £150,000,000, a sum which at the rate of exchange then and now was equal to about $550,000,000, for the purpose of stabilizing exchange rates. The

authority was granted, and what has been known as the Exchange Equalization Fund was established. There was nothing extraordinary about this action. The transactions between Great Britain and the rest of the world are of large importance, and there was no reason why the exchange rates should be left wholly to the chance of day to day fluctuations aggravated as they might be by speculative manipulation at home or abroad. Stabilizing an exchange rate is accomplished by buying or selling foreign currencies (bank credits) as offered, to the extent necessary to keep the rates within the limits fixed upon. Of course, this is either stabilizing your own currency in relation to a foreign currency or fixing the value of the latter in relation to your own, as you or a citizen of the foreign country may choose to call it. That is to say, a country cannot influence its own exchange rates without affecting the exchange rates of other countries.

To begin with, the Fund of course was in sterling, but when dollars were acquired it meant a transfer of so much of the Fund to New York, or if francs were acquired, a similar transfer occurred to Paris. These foreign credits then were available to give in exchange for sterling when the balance of payments might turn against London.

After about the middle of June the dollar-pound rate of exchange rose from the dollar viewpoint, or fell from the pound viewpoint, from about $3.80 to about $3.45 in October, a trend accompanying the return flow of gold to the United States, which began in June and aggregated over $500,000,000 in six months. At about $3.50 or $3.45 the Fund intervened to prevent a further trend in that direction, but seemed to be unable to resist the market forces. The following extract from an editorial in the London Statist of October 29, 1932, gives what seems to have been current opinion upon that situation at the time:

> For some time the dollar rate was kept "pegged" at over $3.45 by ready support from this fund until, about a fortnight ago, the strain of keeping the rate at this level proved too great, the control was withdrawn, and the exchange value of the pound was allowed to find a level more in keeping with the normal forces which had been acting on the exchange markets. Since then, the dollar rate has slumped and touched $3.26 on Thursday of this week (October 27, 1932), but has since made a slight recovery. What remains in the Exchange Equalization Fund after the attempts that were made to support the rate at about $3.45 can only be a matter of conjecture to the general public.

By this time the question whether or not Britain must make a payment to the United States Government in December began to loom up. The pound declined to about $3.15 but recovered rapidly after the announcement that the payment would be made in gold instead of by acquiring exchange.

Bank of England Acquires $300,000,000

In January 1933 a renewal of banking troubles in this country, and of rumors that the country might leave the gold basis, caused another heavy demand for sterling in exchange for dollars. This led to a remarkable development which has been widely misunderstood, to-wit, the acquisition by the Bank of England of something more than $300,000,000 in gold since January 1st. It has been apparent to any one familiar with the exchanges that this was not due to any aggressive action on the part of the Fund managers. A movement to transfer capital from New York to London caused the exchange rate to rise quickly to $3.45, which was the point at which the Fund managers had made their previous attempt at stabilization. Pursuant to this policy they took all of the exchange offered at this rate. This gave them dollars in New York, for which they either earmarked gold at the Reserve Bank, transferred gold to London, or bought other foreign exchange. Their operations were by no means confined to dollars, but were also in francs, and partly in other currencies, all significant of transfers of capital to London. In the aggregate gold to the amount of $307,000,000 was added to the Bank of England reserves from January to April 26, 1933.

Following so soon after the British payment of $95,500,000 to the United States Government on December 15th last, and the attendant publicity, this seemed to be a case of extraordinary replenishment. The Bank of England was possessed of more gold than before! What was the secret of this marvelous recovery?

The explanation is simple, as appears above. Although the gold is in the Bank of England, it does not represent an addition to the wealth of England, but rather a deposit liability of the Bank, which in these times of unsettlement may be withdrawn at any time.

There is no evidence that the operations of the Exchange Equalization Fund or the operations of the Bank previously have been especially related to the dollar exchange, and if reports are correct they have not been signally influential in the long swings. They are understood to have opposed the long rise from $3.45 to $3.83, opposed the decline below $3.45 and opposed the last rise above $3.45, in all of which operations they apparently failed to accomplish the desired objective. This may account for the announcement of the Chancellor of the Exchequer that he would ask for an increase of the Fund.

The Demoralizing Influence of Depreciating Currencies

That the influence of depreciating currencies on world trade is demoralizing upon prices is not questioned, although the extent of the in-

fluence may be exaggerated, and it cannot be accepted as a good reason why a country which has a firmly established monetary system should abandon it in order to participate in competition of this kind.

That the depreciated currencies have to some extent aided imports into the United States cannot be denied, but Mr. Robert L. O'Brien, Chairman of the Tariff Commission, is in a position to have as much real information on this subject as anybody and he has summed up his observations as follows:

> Half the world, let us say, is off the gold standard. It is very severely competing for our market. Half the world is on the gold standard. It, too, is very severely competing for our markets. The articles in which our importations increased in the last year were quite evenly divided between the two types of countries. Only last week we had a hearing on gloves in which the attorney for the higher duties pointed out a sensational increase in imports from Germany—a country on the gold standard.

He also cited wool hats from Italy and steel from Germany, Belgium and Luxemburg, all on the gold standard, as examples to prove that a troublesome increase of importations is not in itself proof of injury from currency depreciation. It is one of the features of a bad situation, and it is a situation that may be made far worse by ill-advised action.

In the years when the German currency was depreciating there was some excitement in this country and elsewhere about the menace of German competition, but the Germans had their own experience with their depreciated currency and despite their present need for exports they do not resort to it. The depreciated currencies of France, Belgium and Italy afforded those countries some trading advantage while they were depreciating, but none of these countries desires to have such an advantage again. They found that the cost of depreciation at home was greater than the benefits they gained abroad.

The trading advantage derived from currency depreciation arises from the fact that the depreciation is effective in a country's exchange rates before it is in internal prices, but the latter gradually are adjusted, as has been the case in the countries named. Such an advantage is abnormal and lasts only while the currency is depreciating. There is no reason to believe that the competition of Great Britain and all of the countries with depreciated currencies could have turned the balance of payments against this country and forced it off the gold basis. That would involve a continuing depreciation beyond any point to which they would be likely to go.

In one respect a great gain has been recently made in an understanding of international relations. The importance of having a common standard of value is now generally recognized. No longer is heard in clarion tones the demand for "an independent monetary system of our own," to be adopted "without the advice or consent of any other nation." The disorder in the exchanges since 1929, and especially since 1931, has demonstrated that such independence for all nations means chaos in trade. There are different systems of weights and measures, but they have fixed relations to each other. The "foot" and the "meter," the "mile" and "kilometer," always mean the same in terms of each other, and an approximate stability existed between monetary units when all currencies were based upon gold. But currencies without a common standard assuring ready convertibility into each other inevitably fluctuate in relation to each other and the fluctuations become a factor in trade. As an instrument of trade rivalry a depreciating currency is a demoralizing form of competition, but of only temporary effect. It is unjustifiable even in self defence, for if left to itself it defeats itself.

The value of a common standard of value has been abundantly demonstrated in the past and the idea of cooperative relations between central banks to give increased stability to credit conditions and prices is entirely sound. Any such system of international management, however, presumably would be for consultation and cooperation only, and without authority over the monetary system of any country. It would not be interested in the composition of the unit dollar of the United States, except as instability in the exchanges might be introduced by altering it. It does not at all matter to the people of the United States that the French unit of value is now of the present composition instead of the pre-war composition. No more or less gold is required for the monetary system of France now than under the pre-war system. The temporary effects of that change upon international trade have practically disappeared, and the effects upon internal relations are exclusively a concern of the French nation.

The 30-Hour Week

The United States Senate has passed a bill for an act to forbid the shipment or transportation in interstate or foreign commerce of any article or commodity "which was produced or manufactured in any mine, quarry, mill, cannery, workshop, factory, or manufacturing establishment situated in the United States, in which any person was employed or permitted to work more than five days in any week or more than six hours in any day." The act would have a time limitation of two years.

A preamble states that millions of people unable to obtain employment "are suffering destitution, undernourishment and want, while millions of others are working in factories and industrial establishments ten, twelve, thirteen, fourteen, and even sixteen hours per day." According to the United States Bureau of

Labor Statistics only 11 per cent of the employes of all manufacturing industries were working more than 48 hours per week in May, 1932, and since this available information indicates that most of these were working on a 10-hour basis or less, little importance need be given to the mention of "twelve, thirteen, fourteen and sixteen hours per day." The latest employment study of the National Industrial Conference Board, covering 1,079 manufacturing establishments with 921,157 rank and file workers on the payrolls as of February 1, 1933, showed an average of 29.6 hours worked per week. These figures for average man-hours are arrived at by dividing the total hours of individual employment by the total number of employes on the payrolls, and since it is the usual practice to share the available work with all persons regarded as regularly attached to an establishment the resulting figures should approximately indicate the relation of current employment to normal employment. If additions to a force were made from the ranks of the wholly unemployed, the average of man-hours would be lowered and of course the average wage distribution would be lowered.

The Restrictive Features

There is no reason for thinking that the law would increase the aggregate man-hours of employment, the design being only to spread out the available employment. On the other hand, there are reasons for thinking that it would have restrictive effects, tending to reduce employment and impede recovery. Since the limitations apply separately to every industrial establishment, it seems certain that to level employment in all industries to not more than thirty hours per week per employe would require very considerable shifting, not only between establishments of different localities but even between different lines of industry. Obviously labor is not so liquid that it can readily flow to a uniform level throughout all industries and all parts of the country.

It is improbable that the cotton goods industry, which the Conference Board's Report shows as operating above an average of 45 man-hours per week could bring single shift operations down to thirty man-hours per week without reducing production and employment, and the same may be said of other important industries reported as operating at an average between 40 and 45 man-hours per week. An excess of employment available in these industries could not be transferred to other lines of industry operating at less than thirty hours per week, (as for example, steel, equipment and construction) and the latter would be injured instead of benefited by restriction of the former.

In short, while the plan might level out employment to some extent within lines of industry, it would not do so across industry lines, and the leveling process within industries might lessen the activity of the more aggressive and efficient establishments.

The necessity for shifting between establishments might be obviated to some extent by operating several six-hour shifts, but this would be impracticable in many cases, or might entail extra expense, either of which would have a restrictive effect. Since there is no prospect that the measure would increase the demand for products, every restriction upon employment would be a net loss.

The most marked effect of the plan would be to cause the doubling, or greater multiplication, of shifts and thus the extension of night operations throughout industry, which heretofore has been opposed on both economic and social grounds. It would seem that if the industries have sufficient capacity to supply the demands upon them by daylight operations—as the advocates of this measure apparently believe—there is no good reason to stimulate night work.

The plan attempts to extend and enforce the practice of spreading work which has been in effect by voluntary agreements between employers and employes, but the latter plan does not restrict the freedom or enterprise of individual establishments and is adaptable at will to changing conditions. This voluntary spreading has been recognized and accepted as an emergency measure, but even so has been open to several serious objections. It reduces wage income without reducing production-costs or living-costs, and therefore without doing anything to stimulate increased consumption or employment. Although it makes a state of large unemployment more endurable, it does nothing to overcome it, tending rather to carry the situation along without change.

The law would increase the complexity of the wage situation. The voluntary arrangements for spreading work have not as a rule caused an increase of wage rates, because the arrangements have been considered temporary and it has been obvious that an increase of costs would result in a further depression of trade and loss of employment, but the establishment of the system by law, with other regulatory features, would naturally cause a demand for higher weekly wages. Since the industries as a whole are not making any profits, the increase of costs would necessitate a general rise of prices and living costs. This would increase the disorder in price relations which is the real cause of the depression and unemployment.

Allow Freedom to Industry

Why should the law seek to restrict any legitimate effort to enlarge the volume of business and of employment? Strenuous efforts are being made to introduce new goods and to lower costs of production and handling in all lines, for the purpose of increasing consumption. Volume of business is an important factor in costs to every establishment and an increase of the physical volume of trade has beneficial effects all along the line, from the producer of raw materials, through the transportation agencies and all processes of conversion to the factories, merchants and consumers. The need is to increase consumption, and this is much more likely to come by the efforts of all the individual industries, each grappling its own problems, and endeavoring to increase its own sales, than by such measures as this.

The Basic Fallacy

The foregoing comments relate to details, but the main objection to the plan is that it is based upon false premises and attacks unemployment in the wrong way. Its supporters are under the influence of the idea, always prevalent when the economic system for any reason has become disorganized, that productive capacity has outgrown consumption demands, or as frequently expressed, has outgrown purchasing power, leaving nothing to do but slow down industry and compel an equitable distribution of employment.

Reflection should suggest that something is wrong in this theory. The preamble of the bill tells of the destitution of millions who have no employment, and it is common knowledge that the average employment of those who are still connected with payrolls does not adequately supply their needs. It is evident that the American people, although possessed of a magnificent industrial equipment, are not using it, outside of agriculture, at more than about one-half of its capacity, and in consequence are suffering great and actually needless privations. This is the fundamental truth upon which attention should be focussed.

It is safe to say that never even in the most prosperous times has any considerable proportion of the people of this country even approached the state of having all their wants satisfied. Furthermore, after every period of arrested industrial development, and incidental revival of this theory of excess capacity, the industries have gone on to larger per capita production, and the standard of living has advanced to higher levels, than ever had been known before.

Can there be any doubt that the wants of the people are sufficient to provide them with all the employment they care to have? It is not an insatiable craving for work in itself that makes the persistent demand for it, but an insatiable craving for the vast variety of goods and services which economic society has learned to supply and taught the people to want, and the production of which provides employment. Thus the real problem in the aggregate is not how to get jobs, but how to get the values which jobs at once create and are the means of obtaining. There is no employment problem apart from supplying wants. As by the increasing productivity of industry the workers find their more pressing wants supplied, they may prefer to have less employment rather than more gratifications, but that is a matter of their own choice and presents no employment problem.

As to purchasing power, there is none outside of the labor, products and services exchanging in trade. They pay for each other. Money, checks, drafts, bills of exchange and bank deposits are simply instruments by which the exchange of real values is carried on. The present unemployment situation, like all other similar situations, has not been caused by any general excess of production over wants, but by a state of disorder in the exchanges.

This view is not new or possessed of any novelty. It is embodied in the teaching of the principles of economics in all the universities of the world.

The Demand for Labor

The Royal Economic Society of London at its last annual meeting elected as its President, Edwin Cannan, Emeritus Professor of Economics of the University of London, long one of its eminent members. He took for the subject of his presidential address "The Demand for Labour," and the address appeared in full in the September, 1932, number of the Society's quarterly publication "The Economic Journal." No doubt he was prompted to his choice of a subject by the state of unemployment and perhaps by the publicity given to "technocracy" about that time.

The opening paragraph of Professor Cannan's address is suggestive, as indicating at once not only his own attitude toward the fears of general unemployment but his understanding of the attitude of his audience. He began almost apologetically, as follows:

If everything were as it should be, The Demand for Labour would be too elementary a subject for me to take in addressing the Fellows of the Royal Economic Society in the forty-second year of its existence. But it is a melancholy fact that the forty-one completed volumes of the Society's Journal have not succeeded in producing any considerable improvement in the mind of the public in connection with this matter. Within the last few years the governments of two great countries have actually congratulated themselves on the fact that the demand for labour had increased along with the increase of population, as if that were something unusual; a British Cabinet Minister supposed to be in charge

of Employment has entreated pensioners and owners of property (other than his wealthy colleagues) to get out of their jobs to make room for the unemployed; and eminent statisticians have found great comfort in the declining growth of population, being apparently under the impression that the smaller the population is, the less likely is it to come up to the amount of employment.

The speaker proceeded in true analytical fashion to reduce economic society to its simplest terms by "asking in the first place what would happen if there were no sort of communication between individuals," continuing as follows, abbreviated:

In that case the number of workers would coincide exactly with the number capable of work, for the very cogent reason that nobody could live without employing himself. Stark necessity would drive every one to work to some extent—in fact, a very considerable extent—and beyond this he would work for just as long as seemed to him worth while. Defoe never depicts his Robinson Crusoe as in want of a job. Nor does he suggest that if there had been a hundred survivors from the wreck instead of only one, they would have sat on the shore and said: "Our teeming population is too great for the work to be done; we must have an eight-hour instead of a ten-hour day, or else put twenty of us on the unemployment register." It might be more difficult for a hundred to subsist on the little island than it was for one, but that would suggest working more rather than less.

Thus by strictly relating each person's job to his own wants and increasing the population of Crusoe's island the speaker illustrates that, other things remaining the same, the task of supplying wants tends to increase rather than diminish as the population increases.

The Division of Labor

At this stage he introduces the division of labor, having the hundred persons arrange to cooperate by dividing themselves between the different kinds of work to be done. Since men differ in abilities they naturally produce values of different kinds, and as Adam Smith long ago said, "have a natural propensity to truck, barter and exchange one thing for another." As this group of 100 gets busy in this manner, Professor Cannan supposes an interruption, and conversation is as follows:

If somebody from our present Ministry of Labour arrived and asked the Directors of the society. "Don't you find it difficult to keep so many people in employment?" they would answer, "Certainly not; we want a lot more things than we have. Of course if we were very much better off than we are, it might not be worth our while to work as hard and as long as we do, but that would not be what you would call a difficulty in finding employment."

The first step toward organized industrial society was taken by the division, or specialization, of labor and the resulting exchange of services. It is needless to describe the resulting gains. Professor Cannan says:

Whether such a society worked under conscious direction—autocratic or democratic—or worked by way of countless individual bargains and contracts, would not matter at all. The system of co-operation by individual agreement could only come into existence gradually, owing to individuals finding that they could get more by exchanging services than by working each in isolation, and we cannot imagine anyone complaining that he had been "thrown out of work" or "deprived of his employment" when he improved his condition by concentrating on a special kind of labour.

The human race always has been in a struggle against scarcity. Only a little more than 100 years ago Thomas Malthus wrote his gloomy essay upon population in which he presented the theory that population tended constantly to press upon the means of subsistence, and that poverty was the inevitable lot of the masses of mankind. It made a tremendous impression because nobody knew enough about the possibilities of increasing production to make an effective reply. The population of Europe at that time was about 180,000,000 and has been estimated at 460,000,000 in 1914. It is certain that if the knowledge of physics, chemistry and the utilization of natural resources was no greater now than in 1800, if methods of industry were the same, and if no improvement in means of transportation had occurred to enable Europe to develop an increased trade with the rest of the world, the growth of population on that continent with the depletion of natural resources, and increased demands upon a limited land area, would have imposed more labor (employment) upon the people, and that the conditions of life would have been harder, not better, on that account. On the contrary the living conditions are much better for the masses in 1933 than they were in 1800. Thus it clearly appears that the real industrial problem never has been primarily that of finding employment for the people but of so organizing and developing industry as to most adequately meet the wants of the people.

The Exchange of Services

It is most important to observe that the fundamental principle upon which industry and business has developed from the beginning is that of an exchange of services. Men began to exchange products and services before monetary systems were thought of, and today the real basis of trade is the relative values of the goods and services being exchanged, determined in the long run by the costs of production in human effort, but from day to day in the markets through their comparative abundance or scarcity and other competitive conditions, as reflected in prices in terms of money. If a given commodity is relatively scarce it tends to rise, or if plentiful tends to fall, in comparison with other commodities, and all its exchange relations are affected. Furthermore, these fluctuations effect an automatic regulation of industry, and it is difficult to see how any other system of control over the vast productive activities of the American people could be as satisfactory as this automatic control resulting from the unhampered action of the producers themselves.

It is evident, however, since the entire distribution of goods and services into consumption is by a system of exchange, that it is highly important to have the varied offerings come forth in approximately balanced relations to each other, in order that the markets may be promptly cleared and congestion avoided. If for any reason the exchanges are interrupted, products will pile up, consumption will decline, prices will fall, unemployment will develop, and the whole interdependent economic system will be deranged, as now seen. The requirement of balanced relations means that the working population must distribute itself among all the industries and occupations in such proportions that the products and services will be offered in due proportions to each other and to consumption demands, and also that they shall be so valued to each other that the accustomed volume of exchanges can be readily made and pass into consumption. If these conditions are not complied with something like a blockade occurs.

Maintaining the Balance

This maintenance of balanced relations between the industries may seem to be a formidable requirement, but Professor Cannan shows that it is not nearly so much so as might be thought. "Of course," he says, "if recruits for the industrial forces should fall down from heaven at the rate of one hundred thousand per week on some small community, and declare that they were skilled mustard-makers and mustard-makers they must always be, they could not be employed," but he describes what really happens as follows:

> If we imagine the recruits arriving, as they do in real life, in the shape of boys and girls spread all over the area, and becoming adolescent workers under the care and influence of their parents and friends, who push them into the various occupations wherever the most promising openings present themselves, we can see that the expansion of the different classes of employment would be sufficiently simultaneous to secure an all-round increased demand for goods and services to meet the increased supply. The additional workers make employment for each other.

He pictures the development and flexibility of the wonderful organization as follows:

> * * * To talk of the thousand million workers in the world as having arranged terms on which they will work for each other, certainly seems a little unreal. Human imagination boggles at the task of conceiving what would happen if we all lost both our memories and our records and had to start afresh, each of us having to come to an agreement with all the others who might want his services or be prepared to serve him. But we never need a fresh start. The beginning was made ages ago when population was sparse and facilities of transport were trifling, so that each man had few neighbours and little chance of serving and being served by people at a distance. It is only by a very gradual process that the little circles within which cooperation was possible have widened till they have cut into each other and produced an organisation which covers the whole earth, and is so complicated that it is quite exceptional for anyone to have more than a vague impression of the thousands of men and women in all parts of the globe who have contributed their mites of labour to the production of the food which he eats and the clothes which he puts on, and it is unusual for anyone to have very much more knowledge of those whom he serves directly and indirectly and who may sometimes be as numerous as those who serve him. Moreover, though the body of persons in economic cooperation cannot, any more than the human body, be resolved into the atoms of which it is composed, and be reconstituted in a new form, old atoms are continually going out of it, and new atoms are continually coming into it, so that the complicated mutual agreement is constantly subject to gradual modification.

Importance of Cooperative Relations

The exchange of services is the theme of Professor Cannan's address. Through it he comes to the cause of unemployment, which he shows is not because of a lack of work to be done, but because at times the system gets out of balance, interfering with the free flow of the exchanges. Referring to his previous illustration of the isolated man he says (italics his own):

> The source of employment remains as in the case of isolated individuals—the desire of man to satisfy his needs. But while the isolated individual satisfies his own needs directly by his own labour, in organized industry each of the associated individuals seeks to satisfy them by the indirect method of satisfying other persons' needs, and having his own satisfied by what he gets from them in exchange. *When they fail to agree in the bargaining, unemployment appears.*

The speaker describes at length the misunderstandings and disagreements which complicate the relations between employers and employes and between the different groups of the economic system. He explains that one of the most important causes of confusion is a prevailing misconception of the function of money. He emphasizes that trade is essentially barter and that money in its common use is not original purchasing power but a means by which different things are measured against each other and exchanged. We quote briefly:

> * * * When a person is offering services to an employer who re-sells to the consumers, it is much less obvious to him that in order to keep in employment he must produce what the consumer wants at a price which the consumer will pay, than it is when he is offering goods or services directly to the consumer.
>
> When nearly all bargains are made in terms of money, and incomes are universally reckoned in money, general illusion is easier and disillusionment is not likely to come so quickly. It becomes much easier to expect more than can be got, and it takes longer to discover the mistake. When A and B, instead of exchanging their products directly, both sell them for money in the market and do not come face to face, their extravagant pretensions are not confronted with each other. Each imagines himself as getting money from an impalpable entity called "the consumer," whom he credits with infinite means of payment, rather than as bartering his own products for the products of other people. The terms on which he parts from his own product depend in fact just as much on the purchasing power of the money he receives as on its amount, but it is very seldom that he fully realizes this. * * * Nearly everyone is more pleased with a rise of 10 per cent in his money-income than he is annoyed by a coincident 10 per cent rise in the price of the things he buys, and nearly everyone is very much more annoyed by a fall of 10 per cent in his money-income than he is pleased by a coincident fall of 10 per cent in the price of the things he buys.

The War Disturbance

Professor Cannan's address is a lucid exposition of the development and ordinary workings of the economic system, but does not enter into the extraordinary conditions arising from the war. Unquestionably, the war has exerted an influence of paramount importance in all developments since July, 1914. Production, trade, wages, prices, credit, money, and all of the relationships of the economic system have been violently disturbed, more than once, for there have been the changes to war conditions and from war to peace conditions. No such upheaval and succession of disturbances had been known to modern life.

In one of the paragraphs quoted above, describing the intricacies of the economic system the speaker says:

> Human imagination boggles at the task of conceiving what would happen if we all lost both our memories and our records and had to start afresh, each of us having to come to an agreement with all the others who might want his services or be prepared to serve him.

Something like the state of confusion thus suggested has resulted from the disorder in production and price relations which has resulted from the war and the reactions that have followed. There is no need to go into details, for they are familiar, but everything that has happened to business, employment and prices since 1929 is fully accounted for by the unbalanced relations in the economic system.

The Remedy

How is the situation to be cleared up? Obviously, normal relations must be restored throughout production and in the markets, so that goods and services will have approximately their accustomed exchange values to each other. There is no reason to doubt that the American people will be eager to buy as much of everything as at any time in the past, if they can buy as they always have, with what they have to sell. The economic system supports itself, supplying its own buying power and consuming its own products. There is no real buying power from outside the economic circle.

When this is fully understood there will be less talk of providing purchasing power to certain groups of the population, regardless of the cost to the rest of the people. A lot of delusive ideas are afloat on this subject. It looked for a time as though no reduction of the cost of government could be made, for obviously nothing could be done without affecting somebody's purchasing power. However, the President and his aids have found ways to reduce expenditures one billion dollars, believing that this amount of purchasing power will count as usefully in the hands of the tax-payers as in the pockets of present recipients.

In considering the maintenance of purchasing power it is important to know where it originates, and what each recipient gives in exchange for the share he claims. Bearing in mind that the real pay of every person for his contribution to the general prosperity comes in the products or services of others, assume that at a given time, say 1913 for example, such exchange relations generally were on a fair basis, having been fixed by the free play of economic forces under normal conditions. On this basis employment would be normal, and production would move steadily into consumption. Suppose that an extraordinary disturbance, as a great war, throws group relations into grave confusion, and instead of attempting to take account of the changes in detail let it be supposed that the community is consolidated into two about equal groups, who can have no trade relations except with each other. Now let it be supposed that one of these groups insists upon terms of exchange which will give it about twice as much of the products of the other group for each unit of its own, as was customary before the upheaval: What will be the effect upon their trade relations? The second group can buy the products of the first only to the extent that its own will make payment; it cannot increase its production for that purpose and the first group would have a surplus of its own products left over, which it could not use, and one-half of its members would be out of employment and bereft of purchasing power.

No such situation can be imagined as occurring if people are trading face to face with each other, but it does occur when they trade indirectly by the use of money and think only of receiving money from an employer or the "market," instead of the trade relations which actually are their vital concern. What has been a mutually satisfactory trade in the past is thus blocked by a change in the price relations, and the results are equally disastrous to both sides.

The trouble is that the reciprocal nature of trade is overlooked. The compensation of the different industrial groups cannot be fixed independent of each other. The compensation of each group comes from the others. A single group may view with indifference the loss of purchasing power in other groups, until it discovers that its own employment and income are dependent upon that purchasing power. Eventually all must learn that this highly organized economic system exists by the exchange of services on equitable terms, and that every group is necessarily concerned not only in fair play for itself but fair play for all the groups in the economic system. The principle of equity underlies all economic law. The economic system does not work unless it is in balance.